FILE COPY

No. 919

IN THE

Supreme Court of the United States

October Term, 1937

RICHARD E. LANG, Executor, and GRACE E. LANG, Executrix, of the Estate of JULIUS C. LANG, Deceased,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

ON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITIONERS' OPENING BRIEF

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ROBERT E. BRONSON,
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JURISDICTION

This proceeding arose through an appeal by the petitioners to the Board of Tax Appeals from a proposed additional assessment of estate taxes (R. 1). The decision of the Board is reported in Volume 34 B. T. A. 337, which is the only opinion herein. The petitioners sought a review of the Board's decision in the Circuit Court of Appeals for the Ninth Circuit, under Section 1001 of the Revenue Act of 1926, as amended by Section 1006A of the Revenue Act of 1932, and Section 1002 of the Revenue Act of 1926, as amended by Section 519A of the Revenue Act of 1934. Following argument to the Circuit Court of Appeals, that court has certified certain questions and propositions of law, under Section 239 of the

Judicial Code, as amended by the Act of February 13, 1925 (R. 5, 7).

STATEMENT OF FACTS

The decedent died December 23, 1929. His estate was subject to the Federal Estate Tax of 1926. There were in force at the time of his death seventeen insurance policies upon his life, aggregating a total in excess of $200,000.00. He had married in 1905, and thereafter, until his death, he and his wife, who survived, were citizens of the State of Washington, a community property state. Fourteen of the policies were applied for after marriage, and the first and all subsequent premiums thereon were paid from community funds. The decedent's wife was the sole beneficiary under eleven of these fourteen policies, and his children were the beneficiaries in the other three. The remaining three policies were issued to decedent before marriage, and the first few premiums thereon were paid by him out of his separate property and the remainder were paid out of community funds, and his wife was beneficiary thereof (R. 1, 2).

The questions presented herein depend on a construction of Section 302(g) of the Estate Tax Act of 1926, as applied to the proceeds of such policies. This section, except for a slight addition made in the Revenue Act of 1934, has been contained in identical terms in the Revenue Acts of 1918 and 1921 (Section 402), and the Revenue Acts of 1924, 1926, 1932 and 1934 (Section 302(g)). It reads as follows, the addition of 1934 being included in brackets:

"Sec. 302 (as amended by Section 404 of the

Revenue Act of 1934). The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated [except real property situated outside the United States] * * *.

"(g) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life * * *."

The pertinent provisions of the statutes of the State of Washington relating to community property, and the Commissioner's regulations issued under the Federal Estate Tax Acts, are set out in appendices to this brief following page 27.

STATEMENT OF QUESTIONS PRESENTED

An original and amended certificate have been submitted herein, which, taken together, seem to present the following problems for solution, based upon the facts set forth in the above statement:

1. In the case of a policy issued after marriage upon the life of a decedent husband, on which all of the premiums were paid with community funds and under which the wife is the sole beneficiary, are all or only one-half of the proceeds, less $40,000.00, to be included in the gross estate? (Questions 1 and 4)

2. In the case of a policy issued, prior to marriage, upon the life of a deeedent husband, the premi-

ums on which were paid before marriage from decedent's separate funds and after marriage from community funds and under which the wife is the sole beneficiary, are all of the proceeds in excess of $40,000.00 to be included in the gross estate or should they be reduced by one-half of that proportion of the total proceeds which premiums paid with community funds bear to total premiums paid? (Questions 2, 3 and 5)

3. In the case of a policy issued after marriage upon the life of a decedent husband, payable to his children as beneficiaries, on which all of the premiums were paid with community funds, should the full amount or only one-half of the proceeds, less $40,000.00, be included in the gross estate? (Question 1, unqualified by Question 4)

PETITIONERS' CONTENTIONS

The petitioners' contentions are as follows:

1. In the case of the policy issued after marriage and payable to the wife, only one-half of the proceeds, less deduction of $40,000.00, should be included in the decedent's gross estate.

2. In the case of the policy issued before marriage in which the wife is the beneficiary, only an amount of the proceeds proportionate to the amount of premiums paid with separate funds to total premiums paid, plus one-half of the remainder, and less deduction of $40,000.00, should be included in the gross estate.

3. In the case of the policy payable to the children, issued after marriage and paid for entirely with community funds, only one-half of the proceeds, less

deduction of $40,000.00, should be included in the gross estate.

SUMMARY OF ARGUMENT

A. The wife's interest in community property under the law of the State of Washington is equal to that of her husband. She owns one-half of any insurance maintained with community funds which cannot be diverted by the husband without her consent.

B. Only the husband's half interest in community property is subject to inclusion in the gross estate.

C. The gross estate under the Federal Estate Tax Act cannot include the wife's property and rights which are not affected by the husband's death.

D. Under the applicable regulations only the insurance paid for by the husband's funds is deemed to have been taken out by him.

E. Irrespective of the regulations, insurance payable to the wife under policies which have been maintained with community funds should, to the extent of one-half thereof, be excluded from the gross estate of the husband.

F. The same principles apply to a policy which has been maintained with community funds under which decedent's children are beneficiaries.

ARGUMENT

In approaching the problems presented, we are handicapped by the fact that in the court below the Commissioner relied solely on the decision of the Ninth Circuit in *Bank of America v. Commissioner*,

90 F. (2d) 981 (R. 3), and did not undertake any discussion of the general principles involved, so that we do not know his position upon them. For this reason it may be that our argument will cover various propositions which will not be disputed.

General Principles

As a foundation for the petitioners' contentions as to the proper answers to be made to the questions submitted, they advance the following propositions:

1. Under the laws of the State of Washington, the marital community is a separate legal entity and a special legal concept, *sui generis*.

> "It was plainly the intention of the legislature, in the session of 1879, in the passage of the chapter denominated 'Property rights of married persons', Code Wash. T., chap. 183, to depart from the common law and breathe into legal existence a distinct and original creation, partaking, somewhat, of the nature of a partnership and of a corporation, but differing in some essentials from both; and this creature is termed a 'community.' "
>
> *Brotton v. Langert*, 1 Wash. 73, at 78, 23 Pac. 688.

See also:

Holyoke v. Jackson, 3 Wash. Ter. 235, 3 Pac. 841;

Warburton v. White, 176 U. S. 484, 20 S. Ct. 404, 44 L. ed. 555;

Graham v. Commissioner, 384 C. C. H. § 9172 (9th Circuit, March 4, 1938).

2. The interests of husband and wife in community property are identical so far as ownership is concerned. The wife's right therein is an absolute and vested one, equal in all respects to that of her husband.

> "In this state * * * as has always been stated by this court, the wife has a vested property right in the community property equal with that of her husband, and in the income of the community, including salary or wages of either husband or wife, or both."
>
> *Occidental Life Insurance Co. v. Powers*, 92 Wash. Dec. 425, at 433, 74 P. (2d) 27.

> "The books are full of expressions such as 'the personal property is just as much hers as his' (*Marston v. Rue*, 92 Wash. 129, 159 Pac. 111, 112); 'her property right in it (an automobile) is as great as his' (*Id.*, 92 Wash. 133, 159 Pac. 111, 113); 'the title of one spouse therein was a legal title, as well as that of the other' (*Mabie v. Whittaker*, 10 Wash. 663, 29 Pac. 172, 175).
>
> "Without further extending this opinion it must suffice to say that it is clear the wife has, in Washington, a vested property right in the community property, equal with that of her husband; and in the income of the community, including salaries or wages of either husband or wife, or both.
>
> "* * * We are of opinion that under the law of Washington the entire property and income of the community can no more be said to be

that of the husband, than it could rightly be termed that of the wife."

Poe v. Seaborn, 282 U. S. 101, 9 A. F. T. R. 51 S. Ct. 58, 75 L. ed. 239.

See also opinion of the Attorney General of the United States in community property cases:

T. D. 3138, 4 C. B. 238;

Schramm v. Steele, 97 Wash. 309, 166 Pac. 634.

3. While the husband has the right of management of the community property under Remington's Revised Statutes § 6892, this is merely a statutory agency created for convenience which does not in any wise elevate his actual proprietary interest in the community estate above that of his wife.

Warburton v. White, 176 U. S. 484, 20 S. Ct. 404, 44 L. ed. 555;

Poe v. Seaborn, 282 U. S. 101, 51 S. Ct. 58, 75 L. ed. 239.

4. A husband has no right either of property or ageny entitling him to alienate the interest of the wife in community property.

Poe v. Seaborn, 282 U. S. 101, 51 S. Ct. 58, 75 L. ed. 239;

In re McCoy's Estate, 189 Wash. 103, 63 P. (2d) 522;

Schramm v. Steele, 97 Wash. 309, 166 Pac. 634, and cases therein cited.

In the last case, the Supreme Court of Washington said:

"The husband is made, by the statute, the manager, not the owner. His management and

control include the power of absolute disposition, but only for the community.

"* * * These considerations make it plain that the statute, in conferring upon the husband the management and control of the community property, though giving him the absolute power of disposition of community personalty, intends no more than to make him the statutory agent of the community."

5. The foregoing principles were recently applied in the case of *Occidental Life Insurance Company v. Powers*, 92 Wash. Dec. 425, 74 P. (2d) 27 (an *en banc* decision rendered December 7, 1937) to a determination of rights in a policy of life insurance issued to the husband after marriage and paid for with community funds, in which the wife was named as beneficiary, with right in the insured to change the beneficiary, which he did in favor of his mother and secretary, to the exclusion of his wife. Declaring that the husband could act only as a statutory agent for the benefit of the community, and that here the transaction was without any consideration to the community, the court held that the change of beneficiary was invalid, not only as to the right of the wife to half the proceeds upon the death of the husband, but as to the entire proceeds. The court states as follows:

"* * * In this state, insurance or the proceeds of insurance are not mere expectancies or choses in action, but are property; and if the premiums are paid by the assets of the community, they constitute community property."

To the same effect, see *In re Brown's Estate*, 124

Wash. 273, 214 Pac. 10, holding that insurance on the husband's life, paid with community funds, is community property and the wife owns one-half thereof; and *Shields v. Barton* (7th Circuit) 60 F. (2d) 351, allocating the community interest in proportion to the amount of premiums paid before and after marriage, in the case of a policy taken out prior to marriage. There are many other cases to the same effect from other states, particularly from California, which it seems unnecessary to cite, as the Washington law is well-settled.

6. Under the Federal Estate Tax Act, the gross estate of a deceased husband includes only his half interest in community property and does not extend to his wife's interest therein.

Estate of Edward F. Sweeney v. Commissioner, 15 B. T. A. 1287;

Coffman-Dobson Bank & Trust Co., Executor, v. Commissioner, 20 B. T. A. 890;

T. D. 3138, 4 C. B. 238, first opinion of Attorney General in community property cases;

Estate of Elizabeth Chavez, 34 N. Mex. 258, 280 Pac. 241, 69 A. L. R. 769, and annotation at 780.

This is recognized in Article 23 of Regulations 70 (1929 Edition) relating to the 1926 Act, as amended by the Act of 1928, in the following language:

> "The entire value of such property is *prima facie* a part of the decedent's gross estate, but as it is not the intent of the statute that there should be so included a greater part or propor-

tion thereof than is represented by an outlay of funds, which, in the first instance, were decedent's own, or more than a fractional part equal to that of the other joint owner where neither had parted with any consideration in its acquirement, facts, which in a given case bring it within any one of the exceptions enumerated in the statute, may be submitted by the executor."

See also Annotations in 383 C. C. H. § 3452.

7. The Federal Estate Tax is an excise tax upon the privilege of transferring or transmitting property by death:

"It follows that unless there is such transfer *from the decedent*—unless there was something which passed from decedent upon death—there has been no transfer; no privilege of transfer has been exercised; and there is nothing which can be subjected to an excise tax on such privilege. Therefore, where life insurance proceeds are involved, the initial inquiry is as to what, if anything, has passed *from the decedent* because of his death."

Walker v. U. S. (Eighth Circuit) 83 F. (2d) 103.

"Where an insured reserved no rights incidental to ownership or control of the policies, so that death transfers nothing to the beneficiary and shifts no economic benefits, there is no transfer within the reach of the taxing power, and such policies are not covered by the statute."

Helvering v. Parker (Eighth Circuit) 84 F. (2d) 838.

In addition to the authorities cited in the foregoing cases, see also *Appeal of Guaranty Trust Company of New York*, 33 B. T. A. 1225.

The Policy Was Not Taken Out by Decedent, as to Wife's Community One-Half

Regulations 70 (1929 Edition) promulgated by the respondent as applicable to Section 302(g) of the 1926 Act, provide in Article 25 that:

> "Insurance is deemed to be taken out by the decedent in all cases where he pays all the premiums, either directly or indirectly, whether or not he makes the application. On the other hand, the insurance is not deemed to be taken out by the decedent, even though the application is made by him, where all the premiums are actually paid by the beneficiary. Where a portion of the premiums were paid by the beneficiary and the remaining portion by the decedent the insurance will be deemed to have been taken out by the latter in the proportion that the premiums paid by him bear to the total of premiums paid."

And Article 28, relating to the valuation of insurance, provides that where the policy is payable to a beneficiary, other than to or for the benefit of decedent's estate, and "* * * only a portion of the premiums were paid by the decedent, the amount to be listed on such schedule is that proportion of the insurance receivable which the premiums paid by the decedent bear to the total premiums paid."

While these provisions were omitted from the 1934 Edition of Regulations 80, in the 1937 Edition of

Regulations 80 there was inserted in Article 25 the following:

> "* * * But in the case of a decedent dying before November 7, 1934 (the date of approval of the 1934 edition of Regulations 80) the provisions of the second paragraph of article 25 of Regulations 70 (1929 edition) will continue to apply."
>
> (The second paragraph of Article 25 referred to includes the portion above quoted from that article.)

The phrase "taken out" has not been defined, except in cases arising under this section of the Estate Tax Act. The interpretation placed thereon by the Commissioner in Regulations 70 was accepted without independent discussion in *Wilson v. Cooks*, D. C. W. D., Missouri, 1931, 52 F. (2d) 692, and *Helvering v. Reybine* (Second Circuit) 83 F. (2d) 215. See also *Appeal of Boston Safe Deposit and Trust Com-Company*, 30 B. T. A. 679 at 687.

Without specific reference to the regulations, the same interpretation was placed upon the statutory language in *Igleheart v. Commissioner* (Fifth Circuit) 77 F. (2d) 704, which affirmed the decision of the Board of Tax Appeals, 28 B. T. A. 888, in which it was said, at page 908:

> "The applicable provisions of the statute should be construed as intending to include all the insurance on a decedent's life in favor of beneficiaries other than his estate which was acquired by him through the expenditure of his own money,

where he has the power to dispose of the proceeds of the insurance at will."

The same situation, arising under the same Act, was the subject of a most thorough and vigorous decision rendered by the Eighth Circuit in *Walker v. U. S.*, 83 F. (2d) 103, where the question presented was identical with that in the present case, except that it involved residents of Minnesota, which is not a community property state, and the premiums paid by the wife were paid from her separate funds. Considering that the wife's proprietary interest in community funds in Washington is equivalent to the wife's ownership of her own funds in Minnesota, we can perceive no distinction between the cases whatsoever, particularly as to the application of Regulations 70. Insofar as the test of beneficial interest or control is concerned, which will be considered later, the present case is much stronger for the petitioners than the *Walker* case, because in the latter the decedent had the right to change the beneficiary and to procure loans, apparently without restriction and for his own interest, which, under the Washington decisions, he could not do, at least as to the wife's community half, without her consent.

In that case the Commissioner questioned the validity of his Regulations 70, Article 25, contending that "taken out by the decedent" means applied for by him, and that section of the Regulations was superseded by the corresponding article of Regulations 80, issued in 1934.

(FOOTNOTE 1.) The 1934 edition of Regulations 80 does not contain the provision inserted in Article 25 of the 1937 edition, to which we have

called attention, stating that Article 25 of Regulations 70, 1929 Edition, will continue to apply in the case of a decedent dying before November 7, 1934.

The court held that upon reason and authority, and considering the legislative history of this provision of the Act, and the Regulations issued thereunder, the interpretation given in Article 25 of Regulations 70 is correct, and the rule there laid down the proper one to be applied, and that only that portion of the proceeds proportionate to the premiums paid by the deceased should be considered as "taken out" by him. No review of this case was sought by the government, and apparently the modification of Article 25 in Regulations 80, 1937 edition, is an acquiescence therein.

Respondent did not contend in his brief in the court below that Regulations 70 were inapplicable or invalid, although such a suggestion was made in argument. If it should be advanced here, the answer to it and the reasons justifying the application of Regulations 70 are fully covered in the *Walker* case.

See also Hughes on Federal Death Tax, §56.

Substantially the same interpretation was placed by the Treasury Department on the statutory phrase "taken out" in Regulations 37 issued under the 1918 Act (Article 32), Article 27 of Regulations 63 issued under the 1921 Act, and Article 25 of Regulations 68 issued under the 1924 Act, providing a uniform course of construction over a period of more than sixteen years during which time the statute was repeatedly re-enacted by Congress without substantial change.

Under such circumstances the administrative interpretation as expressed in the regulations is deemed to have received legislative approval.

National Lead Co. v. U. S., 252 U. S. 140, 40 S. Ct. 237, 64 L. ed. 496;

McCaughn v. Hershey Chocolate Co., 283 U. S. 488, 52 S. Ct. 510, 75 L. ed. 1183;

Helvering v. Bliss, 293 U. S. 144, 55 S. Ct. 17, 79 L. ed. 246.

In the last case, the court said:

> "Moreover, from 1923 to 1932 the Commissioner uniformly ruled that the deduction for charitable contributions was to be taken from net income before computation of the tax and in whole from ordinary net income. The reenactment in later Acts of the sections permitting the deduction indicates Congressional approval of this administrative interpretation."

See also:

Walker v. U. S. (Eighth Circuit) 83 F. (2d) 103;

Mayes v. Paul Jones & Co. (Sixth Circuit) 270 Fed. 121, 129, 130.

A law or a regulation interpreting it should not be applied retroactively to the prejudice of those who have acted in reliance on it in arranging their affairs.

Lewellyn v. Frick, 45 S. Ct. 487, 268 U. S. 238, 69 L. ed. 934;

Bingham v. U. S., 56 S. Ct. 180, 296 U. S. 211, 80 L. ed. 160.

In the court below the respondent relied solely, as stated in the certificate (R. 3), upon the decision of

the Ninth Circuit in *Bank of America v. Commissioner*, 90 F. (2d) 981, affirming the decision of the Board of Tax Appeals in 34 B. T. A. 684. That case, however, is readily distinguishable and is not considered binding by the court, as indicated in its certificate, for two reasons:

In the first place, it was stipulated in that case before the Board, and, therefore, conclusively determined for the purpose of record on appeal "that decedent actually took out the policies on his life." For this reason it was held by the majority opinion that it was doubtful if the Regulations were applicable, the court stating, "Since that fact was stipulated, it would seem that the case was ended when the stipulation was agreed upon."

In the second place, the record did not show who was the beneficiary of the policies, and, therefore, while it appeared that the premiums were paid with community funds, in the absence of information in the record as to the beneficiary, it was not possible to bring the situation within the scope of Article 25, Regulations 70, providing that a policy is deemed not to be taken out by the decedent to the extent that the premiums thereon are paid by the beneficiary. Because of the absence of a showing on that point the majority opinion refused to consider the applicability of Article 25, Regulations 70, saying, "We do not know who the beneficiary was. Therefore the provision is not in question."

It was further suggested in that case that the provisions of local law have no effect in the determination of the question. That view, however, is now

rejected by the court in submitting its certificate (Tr. 4). The expression was not necessary to the decision of the case, and appears to have been given without adequate consideration. While it is true, of course, that the federal law is paramount so far as it goes, and, therefore, controlling in the case of conflict with local rule or statute, this view does not apply where there is no conflict, and particularly where the application of the Federal Act necessarily requires a consideration of property rights and interests to determine its effect.

Sharp Estate, decided March 14, 1938. No. 558. October Term, 1937, 384 C. C. H. § 9184;

Helvering v. Bullard, decided February 28, 1938, 82 L. ed. 572;

Blair v. Commissioner, 300 U. S. 5, 57 S. Ct. 330, 81 L. ed. 465;

Freuler v. Helvering, 291 U. S. 35, 54 S. Ct. 308, 78 L. ed. 634;

Tyler, v. U. S. 281 U. S. 497, 50 S. Ct. 356, 74 L. ed. 991, 69 A. L. R. 758 at 764;

Helvering v. Parker (Eighth Circuit) 84 F. (2d) 838;

Pennsylvania Co., etc. v. Commissioner (Third Circuit) 79 F. (2d) 295, Cert. Den. 296 U. S. 651, 56 S. Ct. 310, 80 L. ed. 463;

Johnstone v. Commissioner (Ninth Circuit) 76 F. (2d) 55, 58;

Levy's Estate v. Commissioner (Second Circuit) 65 F. (2d) 412.

A great many other decisions have recognized and applied the same principle, an outstanding example being *Poe v. Seaborn*, 282 U. S. 101, 51 S. Ct. 58, 75 L. ed. 239, and others of the group of so-called community property cases determining the extent of the income of the taxpayer by the application of the principles of the local law.

The only other court decision bearing directly on this subject is *Newman v. Commissioner* (Fifth Circuit) 76 F. (2d) 449, cert. den. 296 U. S. 600, 56 S. Ct. 116, 80 L. ed. 425. That case arose under the laws of Louisiana and confirmed a decision of the Board of Tax Appeals, 29 B. T. A. 53. The policies had been issued after marriage, premiums paid with community funds, and the beneficiary was the wife, with right of change of beneficiary reserved to the insured. It had been conceded before the Board that the proceeds of the policies formed no part of the community estate, and, in concluding its opinion, the Board stressed particularly that the admission that the premiums were paid out of community income did not necessarily mean that the wife had paid a half thereof, and, therefore, the provisions of Article 25, Regulations 70, were apparently considered inapplicable. The opinion does not discuss the principles involved or the decision of the Board at any length. It said:

> "* * * The tax is not upon the proceeds of the policies; it is not upon the interest to which the beneficiary succeeded at death, but upon *the right of disposition and control* the insured had at death. There was no gift here *inter vivos*. The decedent possessed, until his death, the *full right*

to change the beneficiary. *The tax rests on this fact.*" (Italics ours)

The court considered but expressly refrained from deciding the question of validity of Regulations 70 as applicable to insurance, but held them inapplicable under the Louisiana law, because "the transaction is regarded as a gift from the husband to the wife, and the estate of neither is regarded as having paid the premiums so as to be entitled to reimbursement on account of their payment." The discussion and citations, and particularly the dissenting opinion, indicate that the court considered the interests as in the nature of a joint tenancy and that the husband had a beneficial or property interest in the whole, which sustained the tax. This also was apparently the theory of the Board in the decision of the instant case, as it cited in general support of its holding, ~~77 Fed. 1066,~~ *Lang v. Commissioner*, 289 U. S. 109, 53 S. Ct. 534, 77 L. ed. 1066, and *Levy's Estate v. Commissioner* (Third Circuit) 65 F. (2d) 412; Cf. *Edmonds, Adm., v. Commissioner* (Ninth Circuit) 90 F. (2d) 14. That principle, however, is not applicable to the community property interest of the wife under the laws of the State of Washington.

Joint tenancy with the right of survivorship, which in the case of husband and wife is also known as tenancy by the entirety (30 C. J. 565; Hu[illegible], Federal Death Tax, § 41) has been expressly abolished by statute in the State of Washington. Remington's Revised Statutes, § 1344 (Appendix A). While the community is often referred to as *sui generis*, the rights of the wife are essentially comparable to those

of a tenant in common, and although the statutory right of agency is given to the husband, the wife's right is a vested, individual ownership, which is not enlarged or affected in a substantive sense by the death of the husband. The theory upon which the right of a survivor of a joint tenancy is subject to taxation has no application to this case, where the wife, under the laws of the State of Washington, has an absolute proprietary interest in a community half of the proceeds.

While the *Newman* decision was not noticed in *Walker v. U. S.*, 83 F. (2d) 103, it is completely at variance therewith.

A vigorous dissent was written by Sibley, C. J., in the *Newman case*, 76 F. (2d) 449, and by Wilbur, C. J., in *Bank of America v. Commissioner* (Ninth Circuit) 90 F. (2d) 981, and we urge upon this court the correctness of the views therein expressed.

It is interesting to note that in *Carroll v. Commissioner*, 29 B. T. A. 11, decided only a few days prior to the Board's decision in the *Newman* case, and arising also in Louisiana, it was held that the cash surrender value of policies taken out after marriage by the husband, with proceeds payable to his estate, constitute a community asset, and upon the death of the wife one-half of the cash surrender value should be included in the value of her estate. It seems impossible to reconcile this holding with that in the *Newman* case, and it leads to some significant considerations. Undoubtedly, if the policies in this case had been surrendered the day before death and the proceeds made available prior thereto, one-half there-

of, to the extent premiums were paid with community funds, would belong to the wife by virtue of her community interest, and would not be subject to inclusion in the decedent's estate. It is impossible to see any basis for distinction or for a different result where, instead of receiving the cash surrender value, the proceeds should become payable upon the decedent's death on the following day.

Wife's Interest Was Not Subject to Husband's Control

By the changes made in Regulations 80, Articles 25-28, and by his contentions made in the cases above-noted, the Commissioner has advanced the proposition of basing the tax upon the economic interest, or control, or benefits reserved to the insured, which cease at the time of his death, irrespective of who pays the premiums. This theory requires a consideration of the beneficial rights and interests of the husband and wife under the law of Washington, and of what economic control or interest must be found in the husband, as to the wife's community half, to justify the application of the rule.

Hughes, on Federal Death Tax, § 67, p. 111, says:

> "The established administrative policy of the Department as evidenced in its Regulations, the constant re-enactment by Congress of revenue acts with knowledge of those regulations constituting an approval thereof, together with uniform Court and Board decisions so holding, establish that insurance in which the insured has reserved none of the incidents of ownership is not taxable."

In Regulations 80, Article 25, respondent defines the legal incidents of ownership of insurance as including "the right of the insured or his estate to its economic benefits, the power to change the beneficiary, to surrender or cancel the policy, to assign it, to revoke an assignment, to pledge it for a loan, or to obtain from an insurer the surrender value of the policy, etc." If none of such incidents of ownership were retained by the deceased, there would be nothing to support the tax on the proceeds. *Heiner v. Donnan*, 285 U. S. 312, 52 S. Ct. 358, 76 L. ed. 772, which applies by analogy *Hoeper v. Tax Commission*, 284 U. S. 206, 52 S. Ct. 120, 76 L. ed. 248, as forbidding the imposition of the tax where measured by or based upon the value of property in which the taxpayer had no interest or control for his own benefit. A tax so levied would be violative of the Fifth Amendment.

The tax is laid upon the transfer or shifting of an economic interest or control from the decedent occasioned by his death.

> "It is of significance, although not conclusive, that the only section imposing the tax, section 401, does so on the net estate of decedents and that the miscellaneous items of property required by section 402 to be brought into the gross estate for the purpose of computing the tax, unless the present remainders be an exception, are either property transferred in contemplation of death or property passing out of the control, possession or enjoyment of the decedent at his death. They are property held by the decedent in joint tenancy or by the entirety, property of another

subject to the decedent's power of appointment and insurance policies effected by the decedent on his own life, payable to his estate or to others at his death."

Reinecke v. Northern Trust Co., 278 U. S. 339, 49 S. Ct. 123, 73 L. ed. 410.

It is the termination of the power of control or disposition of rights under the policy or to the proceeds thereof or the freeing of the interest of the beneficiary from the control of the insured that justifies inclusion of the proceeds in the gross estate. In *Chase National Bank v. U. S.*, 278 U. S. 327, 49 S. Ct. 126, 73 L. ed. 405, it is said that:

"* * * it is the termination of the power of disposition of the policies by decedent at death which operates as an effective transfer and is subject to the tax."

If no interest passes to the beneficiary as a result of the death of the insured, there is no basis for inclusion of the proceeds in the gross estate. *Bingham v. U. S.*, 56 S. Ct. 180, 296 U. S. 211, 80 L. ed. 160, approving *Bingham v. U. S.*, 7 Fed Supp. 907. In *Levy's Estate v. Commissioner* (Second Circuit) 65 F. (2d) 412, the court applied such principles to exempt from inclusion in the gross estate the proceeds of policies payable to the wife in which, under the law of New York, her interest could not be affected without her consent. The case is similar with respect to the wife's proprietary interest in her community half of the insurance in this case.

To the same effect as applied to tenancy by the entirety see *Tyler v. U. S.*, 281 U. S. 497, 50 S. Ct. 356,

74 L. ed. 991, 69 A. L. R. 758; *Levy v. Wardell*, 258 U. S. 542, 42 S. Ct. 395, 66 L. ed. 758; and *Shukert v. Allen*, 273 U. S. 545, 47 S. Ct. 461, 71 L. ed. 764.

As to the policy taken out before the decedent's marriage in 1905 and therefore long prior to the Estate Tax Act, it is doubtful if the proceeds are subject to the Act and to inclusion in the gross estate to any extent under the doctrine of *Lewellyn v. Frick*, 268 U. S. 238, 45 S. Ct. 487, 69 L. ed. 934, and *Bingham v. U. S.*, 296 U. S. 211, 56 S. Ct. 180, 80 L. ed. 160. See also Hughes on Federal Death Tax, § 62, p. 104-5; *Industrial Trust Co. v. U. S.*, 296 U. S. 220, 56 S. Ct. 182, 80 L. ed. 191, and *Wyeth v. Crooks*, 33 F. (2d) 1018.

Under the settled principles of community property law of the State of Washington, the wife has a vested, equal interest in the policy and proceeds of insurance so far as paid for with community funds. As to her share, the husband has no right or interest of his own but is only the statutory agent to manage the common property for the benefit of the community. As against the wife's interest, he has none of the legal incidents of ownership defined in Regulations 80, Article 25. It necessarily follows that as to the wife's half, no transfer, generation of new rights or interest, or removal of restrictions or control results from the death of the husband which will sustain the inclusion of her community interest in his gross estate.

For the above reasons, therefore, it necessarily follows that there should be excluded from the husband's gross estate one-half of the proceeds of the

policy on which the premiums were entirely paid with community funds, and as to the policy taken out before marriage, one-half of so much of the proceeds as is in proportion to the amount of premiums paid after marriage with community funds.

Policy Payable to Children Not Part of Husband's Estate to Extent of Wife's Community Interest

The foregoing disposes of the questions arising under policies in which the wife is the beneficiary. There is left for consideration the case of a policy payable to the decedent's children, premiums on which have been maintained with community funds. While the provisions of Article 25 of Regulations 70 are not strictly applicable, because the beneficiary has not paid the premiums, the result under the rule of economic interest and incidents of ownership should be the same and only one-half thereof should be included in the decedent's estate, subject to deduction of $40,000.00. In such case one-half of the premiums have been paid by the wife and not by the decedent. One-half of any interest, right, control and power of disposition belong in a substantive sense to her and are not subject to the will of the husband for his own benefit any more than in the case of the policy where she is the beneficiary. Such a policy is not within the scope of the cases sustaining the tax on insurance created by the deceased and subject to his control, or of Article 23 of the Regulations defining the intent of the statute as restricted to such part or proportion as "is represented by an outlay of funds, which, in the first instance, were decedent's own."

The situation in such a case is no different than if half of the insurance had been applied for and maintained by an entire stranger acting through the decedent as his agent.

CONCLUSION

Upon application of the foregoing principles, petitioners submit that the answers to the questions propounded should be as follows:

Question No. 1: One-half.
Question No. 2: No.
Question No. 3: Yes.
Question No. 4: Yes.
Question No. 5: Yes.

Respectfully,

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ROBERT E. BRONSON,
Counsel for Petitioners.

APPENDIX A

Provisions of Remington's Revised Statutes of Washington, relating to property interests of husband and wife:

§ 6890. *Separate property of husband.* Property and pecuniary rights owned by the husband before marriage, and that acquired by him afterward by gift, bequest, devise or descent, with the rents, issues and profits thereof, shall not be subject to the debts or contracts of his wife, and he may manage, lease, sell, convey, encumber, or devise, by will, such property without the wife joining in such management, alienation, or encumbrance, as fully and to the same effect as though he were unmarried.

§ 6891. *Separate property of wife.* The property and pecuniary rights of every married woman at the time of her marriage, or afterward acquired by gift, devise, or inheritance, with the rents, issues, and profits thereof, shall not be subject to the debts or contracts of her husband, and she may manage, lease, sell, convey, encumber or devise by will such property, to the same extent and in the same manner that her husband can, property belonging to him.

§6892. *Community property defined—Husband's control of personalty.* Property, not acquired or owned as prescribed in the next two preceding sections, acquired after marriage by either husband or wife, or both, is community property. The husband shall have the management and control of community personal property, with a like power of disposition as he has of his separate personal property, except he shall not devise by will more than one-half thereof.

§ 6893. *Community realty, conveyance of, etc.* The husband has the management and control of the community real property but he shall not sell, convey, or encumber the community real estate, unless the wife join with him in executing the deed or other instrument of conveyance by which the real estate is sold, conveyed, or encumbered, and such deed or other instrument of conveyance must be acknowledged by him and his wife: Provided, however, that all such community real estate shall be subject to the liens of mechanics and others for labor and materials furnished in erecting structures and improvements thereon as provided by law in other cases, to liens of judgments recovered for community debts, and to sale on execution issued thereon.

§ 6897. *Tenancy in dower and by curtesy abolished.* No estate is allowed the husband as tenant by curtesy, upon the death of his wife, nor is any estate in dower allotted to the wife upon the death of her husband.

§ 6898. *Liberal construction.* The rule of common law that statutes in derogation thereof are to be strictly construed has no application to this chapter. This chapter establishes the law of the state respecting the subject to which it relates, and its provisions and all proceedings under it shall be liberally construed with a view to effect its object.

§ 1344. *Survivorship between joint tenants abolished.* If partition be not made between joint tenants, the parts of those who die first shall not accrue to the survivors, but descend, or pass by devise, and shall be subject to debts and other legal charges, or

transmissible to executors or administrators, and be considered, to every intent and purpose, in the same view as if such deceased joint tenant had been tenants in common: Provided, that community property shall not be affected by this section.

APPENDIX B

Regulations 70 (1929 edition) relating to Estate Tax under the Revenue Act of 1926:

GROSS ESTATE—INSURANCE

Sec. 302. The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated— * * *

(g) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life. * * *

Art. 25. *Taxable Insurance.*—The statute provides for the inclusion in the gross estate of insurance taken out by the decedent upon his own life, as follows: (a) All insurance receivable by, or for the benefit of, the estate; (b) all other insurance to the extent that it exceeds in the aggregate $40,000.

The term "insurance" refers to life insurance of every description, including death benefits paid by

fraternal beneficial societies, operating under the lodge system. Insurance is deemed to be taken out by the decedent in all cases where he pays all the premiums, either directly or indirectly, whether or not he makes the application. On the other hand, the insurance is not deemed to be taken out by the decedent, even though the application is made by him, where all the premiums are actually paid by the beneficiary. Where a portion of the premiums were paid by the beneficiary and the remaining portion by the decedent the insurance will be deemed to have been taken out by the latter in the proportion that the premiums paid by him bear to the total of premiums paid.

Art. 26. *Insurance in favor of the estate.*—The provision requiring the inclusion in the gross estate of all insurance receivable by the executor, without any deduction, applies to policies made payable to the decedent's estate or his executor or administrator, and all insurance which is in fact receivable by, or for the benefit of, the estate. It includes insurance taken out to provide funds to meet the estate tax, and any other taxes or charges which are enforceable against the estate. The manner in which the policy is drawn is immaterial so long as there is an obligation, legally binding upon the beneficiary, to use the proceeds in payment of such taxes or charges. Where the decedent took out insurance in favor of another person or corporation as collateral security for a loan or other accommodation, and either directly or indirectly paid the premiums thereon, the insurance is deemed to be receivable for the benefit

of the estate. The amount of the loan outstanding at decedent's death, with interest accrued thereon to that date, will be deductible in determining the net estate. (See Art. 29.)

Art. 27. *Insurance receivable by other beneficiaries.*—All insurance in excess of $40,000 receivable by beneficiaries other than the estate, regardless of when taken out, must be included in the gross estate where the decedent during his life retained legal incidents of ownership in the policies of insurance, as, for example, a power to change the beneficiary, to surrender or cancel the policies, to assign them, to revoke an assignment of them, to pledge them for loans, or to dispose otherwise of them and their proceeds *for his own benefits*, etc.

However, irrespective of the retention of such legal incidents of ownership, all insurance in excess of $40,000 receivable by beneficiaries other than the estate must be included in the gross estate (1) of any decedent dying after the enactment of the Revenue Act of 1924, where such insurance was taken out, or the beneficiary receiving the proceeds was named, after the enactment of the Revenue Act of 1918, and (2) of any decedent dying after the passage of the Revenue Act of 1918, but before the effective date of Title III of the Revenue Act of 1924, where such insurance was taken out, or the beneficiary receiving the proceeds was named, after the enactment of the particular revenue act in force and effect at the time of such a decedent's death.

The estate is entitled to only one exemption of $40,000 upon insurance receivable by beneficiaries

other than the estate. For example, if the decedent left life insurance payable to three such beneficiaries in amounts of $10,000, $40,000, and $50,000 (total, $100,000), the full amount should be listed on the return and therefrom subtracted the $40,000 exemption as provided in Schedule C of Form 706. The word "beneficiaries," as used in reference to the $40,000 exemption, means persons entitled to the actual enjoyment of the insurance money.

Art. 28. *Valuation of insurance.*—The amount to be returned where the policy is payable to or for the benefit of the estate is the amount receivable. Where the proceeds of a policy are payable to a beneficiary other than to or for the benefit of the estate, and all the premiums were paid by the decedent, the amount to be listed on Schedule C of the return is the full amount receivable, but where the proceeds are so payable *and only a portion of the premiums were paid by the decedent, the amount to be listed on such schedule is that portion of the insurance receivable which the premiums paid by the decedent bear to the total premiums paid.* In cases where the proceeds of a policy are made payable to the beneficiary in the form of an annuity for life or for a term of years, the present worth of the annuity at the time of death should be included in the gross estate. For the method of computing the value of such an annuity, see Article 13, subdivision (10). Where the insurance contract gives the right to receive a fixed sum of money in lieu of an annuity, or other optional settlement, this fixed sum represents the value of the insurance for the purpose of the tax.

Regulations 80 (1937 Ed.) relating to Estate Tax under the Revenue Acts of 1926 and 1932, as amended.

Sec. 302 (as amended by section 404 of the Revenue Act of 1934). The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated [except real property situated outside the United States—] * * *

(g) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life. * * *

Art. 25. *Taxable insurance.*—The statute provides for the inclusion in the gross estate of insurance taken out by the decedent upon his own life, as follows: (*a*) All insurance receivable by, or for the benefit of, the estate; (*b*) all other insurance to the extent that it exceeds in the aggregate $40,000.

The term "insurance" refers to life insurance of every description, including death benefits paid by fraternal beneficial societies, operating under the lodge system. Insurance is considered to have been taken out by the decedent, whether or not he made the application, if he acquired the ownership of, or any legal incident thereof in, the policy; but in the case of a decedent dying before November 7, 1934 (the date of approval of the 1934 edition of Regulations 80), the provisions of the second paragraph of article 25 of

Regulations 70 (1929 edition) will continue to apply. Legal incidents of ownership in the policy include, for example: The right of the insured or his estate to its economic benefits, the power to change the beneficiary, to surrender or cancel the policy, to assign it, to revoke an assignment, to pledge it for a loan, or to obtain from the insurer a loan against the surrender value of the policy, etc.

Art. 26. *Insurance in favor of the estate.*—The provision requiring the inclusion in the gross estate of all insurance receivable by the executor, without any exemption, applies to policies made payable to the decedent's estate or his executor or administrator, and all insurance which is in fact receivable by, or for the benefit of, the estate. It includes insurance taken out to provide funds to meet the estate tax, and any other taxes or charges which are enforceable against the estate. The manner in which the policy is drawn is immaterial so long as there is an obligation, legally binding upon the beneficiary, to use the proceeds in payment of such taxes or charges. If the decedent took out insurance in favor of another person or corporation as collateral security for a loan or other accommodation, the insurance is considered to be receivable for the benefit of the estate. The amount of the loan outstanding at decedent's death, with interest accrued thereon to that date, will be deductible in determining the net estate. (See article 29).

Art. 27. *Insurance receivable by other beneficiaries.*—The statute requires the inclusion in the gross estate of the decedent of the proceeds of any policy, or the aggregate proceeds of all policies, not receivable by or

for the benefit of decedent's estate, to the extent that such proceeds exceed $40,000, regardless of when the policy was or the policies were issued, if the decedent possessed at the time of his death any of the legal incidents of ownership.

The estate is entitled to only one exemption of $40,000 upon insurance receivable by beneficiaries other than the estate. For example, if the decedent left life insurance payable to three such beneficiaries in amounts of $10,000, $40,000, and $50,000 (total, $100,000), the full amount should be listed on the return and therefrom subtracted the $40,000 exemption as provided in the appropriate schedule of Form 706. The word "beneficiaries," as used in reference to the $40,000 exemption, means persons entitled to the actual enjoyment of the insurance money.

Art. 28. *Valuation of insurance.*—The amount to be returned if the policy is payable to or for the benefit of the estate is the amount receivable. If the proceeds of a policy are payable to a beneficiary other than to or for the benefit of the estate, the amount to be listed in the appropriate schedule of the return is the full amount receivable. (For taxable portion see article 27). In case the proceeds of a policy are made payable to the beneficiary in the form of an annuity for life or for a term of years, there should be listed in the appropriate schedule of the return the one sum payable at death under an option which could have been exercised either by the insured or by the beneficiary, or if no option was granted, the sum used by the insurance company in determining the amount of the annuity. * * *